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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Price Cap Performance Review)	Docket No. 94-1
for Local Exchange Carriers)	
)	
Access Charge Reform)	Docket No. 96-262
)	

AT&T OPPOSITION TO PETITIONS FOR RECONSIDERATION

Mark C. Rosenblum
Peter H. Jacoby

295 North Maple Avenue
Room 3250J1
Basking Ridge, NJ 07920
(908) 221-4243

Jules M. Perlberg

One First National Plaza
Chicago, IL 60603
(312) 853-7439

Attorneys for AT&T Corp.

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SUMMARY

Two petitions for reconsideration, filed by Cincinnati Bell Telephone Company ("CBT") and Citizens Utilities Company ("Citizens"), request the Commission to set a lower X-Factor for small (rural) and mid-size LECs. These petitioners argue that the Commission determined its new X-Factor on the basis of studies of larger LECs subject to mandatory price caps, and the productivity results for these larger carriers are "inappropriate" for the small and mid-size LECs.

The Commission has considered and rejected these same arguments in previous price cap decisions. As the Commission stated, it questioned the reliability of the studies submitted by independent LECs attempting to show a lower X-Factor in their individual circumstances, and it found that there was no valid basis upon which to conclude that the studies of individual carriers would be representative of the productivity for small and mid-size carriers as a class. The Commission's solution -- which is just as appropriate today -- was to adopt a uniform X-Factor applicable to all price cap LECs, but to give the small and mid-size LECs the option of deciding for themselves whether to elect price cap regulation.

CBT and Citizens have made no showing that would justify a reversal of the Commission's well-reasoned past policies. These petitioners have not demonstrated that their data on an individual carrier's productivity are

representative of an entire class of small or mid-size LECs, nor have the petitioners presented any special factors related to their particular circumstances that would justify their receiving an exemption from the application of the Commission's newly determined X-Factor.

Accordingly, the CBT and Citizens petitions for reconsideration should be denied.

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AT&T OPPOSITION TO PETITIONS FOR RECONSIDERATION

Pursuant to Section 1.429(f) of the Commission's Rules, 47 C.F.R. § 1.429(f), AT&T Corp. ("AT&T") hereby opposes the petitions for reconsideration of the Commission's Fourth Report and Order in CC Docket No. 94-1 and Second Report and Order in CC Docket No. 96-272, released May 21, 1977, FCC 97-159 (hereinafter "Order" or "X-Factor Order"), filed by Cincinnati Bell Telephone Company ("CBT") and by Citizens Utilities Company, on behalf of itself and its local exchange subsidiaries ("Citizens").

CBT and Citizens ask to be exempted from application of the Commission's newly determined X-Factor, on the ground that they should not be classified along with the larger local exchange carriers ("LECs"). CBT complains that the 6.5 percent X-Factor is "inappropriate" for CBT and "other mid-size LECs" that may elect price cap regulation. CBT Pet. at 1-2. Thus, CBT argues that the 6.5 percent X-Factor should be set lower when applied to

it and other "elective price cap carriers." Citizens takes a similar position on behalf of the rural price cap LECs.¹ Its petition asks that the Commission suspend the application of the 6.5 percent X-Factor to the rural price cap LECs; that a new rulemaking proceeding be instituted to determine an X-Factor specially tailored to the rural LECs; and that, during the pendency of any new rulemaking, the Commission should apply one or all of its former (interim) X-Factors to the rural price cap LECs. Citizens Pet. at 5, 18-19.²

The central argument of both CBT and Citizens is that the Order's productivity offset was determined on the

¹ Because, as Citizens concedes (Pet. Att. 2 at 5), its affiliated LECs are the only rural LECs subject to price cap regulation, it is speaking only for its own interests when it seeks relief on behalf of "the rural price cap LECs."

² Citizens made no submission in the current LEC price cap rulemaking, in response to the Commission's request for comments in the Fourth Further Notice of Proposed Rulemaking, CC Docket No. 94-1, 10 FCC Rcd 13659 (1995). See Citizens Pet. at 6. Moreover, Citizens' petition for reconsideration does not comply with the Commission's Rules in two respects: (1) its petition, including attachments, is well over 50 pages, more than double the 25-page limit specified in the Rules (see 47 C.F.R. § 1.429(d)); and (2) its petition relies, in part, on facts which occurred prior to its last opportunity for filing in this proceeding or which could have been known to petitioner prior to such opportunity (see 47 C.F.R. § 1.429(b)). Because the lengthy attachments to Citizens' petition include evidentiary material that should have been submitted according to the filing schedule in this proceeding, AT&T believes such material to be outside the proper scope of a reconsideration petition, and thus it will

basis of data from the larger, mandatory price cap LECs, specifically the Regional Bell Operating Companies ("RBOCs"), and that this determination is not applicable to the small or mid-size LECs. CBT asserts, for example, that it is unlike the RBOCs because it serves a "single metropolitan area," and it does not have the same scale and scope economies, as well as service mix, as do the RBOCs. CBT Pet. at 3. Citizens claims that "rural LECs share none of the characteristics of the more typical price cap LECs, such as the BOCs or GTE," and hence it should not be "swept up into" a single X-Factor regime. Citizens Pet. at 6. Both CBT and Citizens present various computations, narratives and other data purporting to show that a different (and lower) X-Factor should be applied to them on an individual basis. See, e.g., CBT Pet., App.; Citizens Pet., Atts. 1, 2.

ARGUMENT

THE PETITIONS OF CBT AND CITIZENS SEEKING LOWER X-FACTORS FOR SMALL AND MID-SIZE LECs SHOULD BE DENIED.

These pleas for special price cap treatment made by CBT and Citizens should be denied. Essentially the same arguments were considered by the Commission on at

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not present herein any detailed analysis of these data submitted with Citizens' petition.

least two occasions in the past, and each time these arguments were rejected by the Commission. The same conclusion should be reached with respect to the instant petitions of CBT and Citizens.

First, in the price cap order immediately preceding this one, when the Commission set the interim X-Factor in CC Docket No. 94-1, the Commission concluded that "the productivity adjustment in the LEC price cap formula should continue to be based on an industry-wide measure of productivity." See Price Cap Performance Review for Local Exchange Carriers, First Report and Order, CC Docket No. 94-1, 10 FCC Rcd 8961, 9027 (¶ 146) (1995) (emphasis added). The Commission based its conclusion on its finding that this approach would best replicate the incentives provided in a competitive environment. Id. Significantly, the Commission explicitly rejected arguments, similar to those advanced here by CBT and Citizens, that "the RBOCs are not a valid proxy for the entire LEC industry" for measuring LEC productivity. Id., 10 FCC Rcd at 9027-28 (¶ 147). Accordingly, the Commission decided that the X-Factor in the LEC price cap plan should be determined on an industry-wide basis. Id.

Second, in initially formulating the basic framework for LEC price cap regulation, the Commission provided a thorough and well-considered analysis of the reasons why it decided not to adopt separate X-Factors

tailored to the small and mid-size LECs. See Policies and Rules Concerning Rates for Dominant Carriers, Second Report and Order, 5 FCC Rcd 6786, 6799-6801(¶¶ 103-119) (1990). This same reasoning is fully applicable today and represents a valid response to the points raised in the CBT and Citizens petitions.

As the Commission determined, the most reasonable course to follow was to make price caps mandatory only for the RBOCs and the GTE operating companies, and allow price cap regulation to be voluntary for the small and mid-size LECs. In reaching this conclusion, the Commission observed that (1) it questioned the reliability of the studies (including those performed by CBT) purporting to show a lower productivity factor for the mid-size LECs, and (2) because of the significant diversity among the various independent LECs, it could not assume that these studies of individual LECs should "serve as a model to predict accurately the future productivity of mid-size LECs as a class." *Id.*, 5 FCC Rcd at 6799-6800 (¶¶ 105-112).

This same evaluation is relevant to the data proffered by CBT and Citizens in support of their reconsideration petitions. Although CBT offers a productivity analysis applicable to CBT on an individualized basis, it makes no showing that the results obtained for CBT alone are representative of mid-size carriers as a class or the other "elective price cap

carriers" for whom CBT seeks relief.³ Similarly, there is no demonstration that the data submitted by Citizens are representative of the productivity for "all rural LECs" as a class.

In view of the considerable difficulties of performing productivity analyses for the many individual small and mid-size LECs and the fact that these study results cannot not practically serve as a model for uniform treatment of small and/or mid-size LECs as a class (or classes), the Commission determined that it would not be administratively feasible to establish separate X-Factors for the broad classifications of smaller, independent LECs. This led to the Commission's "decision to grant mid-size and smaller companies the option of voluntarily participating in price caps." *Id.*, 5 FCC Rcd at 6800 (¶ 114).

³ Indeed, CBT goes to great lengths in attempting to demonstrate that its service area is unique and that its operating characteristics differ from those of other LECs. This alone casts serious doubt on any claim that CBT's productivity results are indicative of those for all other "elective price cap" LECs. As the Commission found with respect to CBT's previously submitted study in the initial LEC price cap proceeding, "since the fundamental forces that will define the productivity of CBT and any other company are so different, the basis for the development of a single productivity factor for all small and mid-size LECs is not obvious from CBT's study [T]he experience of a single mid-size company cannot, under these circumstances, reasonably form the basis for a policy judgment affecting an entire segment of the industry." *Id.*, 5 FCC Rcd at 6800-01 (¶ 117) (emphasis added).

The course consistently followed by the Commission since the inception of the LEC price cap plan continues to be a reasonable resolution under present conditions. There has been no material change in circumstances to justify modifying this approach under today's conditions. It is still not administratively feasible to measure separately the productivity of the numerous small and mid-size LECs, nor is there a valid basis upon which to treat individual LEC productivity results as representative of broad classes of these numerous and diverse carriers. Accordingly, there are sound reasons to avoid applying separate X-Factors to the small and mid-size LECs. Rather, the appropriate course is to allow each of the independent LECs to make a voluntary decision, based on its assessment of its own operations, about whether to be subject to price caps.

Neither CBT nor Citizens has made a sufficient showing of material changes in conditions during recent years to justify reversing past Commission policies, which applied the same X-Factors to all price cap LECs, whether large, mid-size, or small.⁴ Nor have these petitioners

⁴ Citizens argues that application of the 6.5 percent X-Factor to rural LECs is "inconsistent" with the universal service goals adopted by Congress in the Telecommunications Act of 1996. See Citizens Pet. at 10-15. It is difficult to accept, however, that the application of a higher X-Factor, which results in lower access charges and lower interstate long-distance rates, would detract from achieving the universal

provided any sound reason for the Commission to alter its policy of giving the small and mid-size LECs the opportunity to decide for themselves whether price cap regulation is appropriate in their individual circumstances.

Indeed, neither CBT nor Citizens has provided a convincing explanation of why each recently decided to operate under price caps -- especially when each has expressed serious misgivings about the application to them of a higher X-Factor, and each knew or should have known about this distinct possibility. CBT made a deliberate choice to elect price cap regulation for itself in the ensuing 1997-98 tariff year. Significantly, it made this election, pursuant to requesting and receiving special permission from the Commission, on June 16, 1997 -- more than one month after the Commission's adoption of the X-Factor Order. See CBT Pet. at 2. CBT admits that it had full knowledge of the 6.5 percent X-Factor at the time it made its election. Id. Given the fact that CBT's position had been consistently rejected in past Commission orders, CBT could not have reasonably entertained an expectation that it would succeed in obtaining a lower X-Factor for itself. Yet it made a conscious decision to

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service objectives of making telecommunications service more affordable and more accessible.

proceed with price caps, well aware of all the implications of that choice.⁵

In short, CBT cannot have it both ways. As a mid-size carrier, CBT was given the option, in the first instance, to elect whether to be subject to price cap regulation. But once having made this election, CBT cannot insist on remaining a price cap carrier, and at the same time expect to be exempted from application of the currently prescribed level of the X-Factor adjustment.

In the case of Citizens, it decided on behalf of its affiliated LECs to be subject to price cap regulation, effective with its tariff filing of July 1, 1996. See Citizens Pet. at 6. Although Citizens made its price cap election prior to the X-Factor Order, it knew at the time that it was already subject to the same X-Factor treatment as the other price cap LECs, that the then-existing

⁵ CBT claims that it "had to elect" price cap regulation in order to gain certain competitive advantages associated with the Commission's recent Access Reform Order. CBT Pet. at 2-3. However, it does not specify why it somehow felt induced to elect price caps, nor does it explain why CBT's competitive situation is more intense than that of the large mandatory price cap LECs, as it contends. Id. Further, CBT does not identify the particular aspects of the Access Reform Order which it found so attractive for its competitive purposes. In any event, the fact remains that CBT determined that the benefits of being a price cap carrier outweighed the obligations (including the X-Factor requirement), and it made this decision fully cognizant of the higher X-Factor level to which it would be subject. CBT's attempt to excuse its price cap election does not constitute a valid justification that entitles it to a lower X-Factor.

X-Factor was only "interim," and that there was a distinct possibility that a higher X-Factor would be adopted in the pending LEC price cap proceeding.⁶ Citizens does not describe any special circumstances influencing it to make its price cap election as of mid-1996.⁷ However, given the status of this proceeding, the likelihood of a Commission decision by the date of the 1997 LEC access tariff filings, and the clear possibility of a significant increase in the interim X-Factor, Citizens had to be fully

⁶ Indeed, well before July 1, 1996, various parties in the LEC price cap proceeding submitted studies indicating a much higher level above the LECs' interim X-Factor. For example, AT&T's study of LEC total factor productivity, filed in March 1996, produced an interstate-only X-Factor of 7.8 percent (including a consumer productivity dividend). See AT&T Reply at 38-39; X-Factor Order, ¶ 36. And by March 1996, the Ad Hoc Telecommunications Users Committee proposed an X-Factor of 9.4 percent, and submitted other studies showing X-Factors as high as 7.3 and 7.9 percent (excluding a consumer productivity dividend). See X-Factor Order, ¶ 37 and n.72.

⁷ While Citizens does not disclose its full rationale for electing price cap regulation as of July 1, 1996, it apparently found it advantageous to do so in view of an expected sharp rise in its earnings later in 1996. According to Citizens' own figures, its rate of return increased markedly beginning in July 1996. Thus, its rate of return (on a pre-sharing basis) increased to 15.02 percent in the last half of 1996 and 16.13 percent in the first half of 1997, averaging to 15.57 percent for the 1996-97 tariff year. On a post-sharing basis, its rate of return averaged 13.65 percent for the 1996-97 tariff year. See Citizens Pet., Att. 2 at 7. These return levels, achieved by Citizens in its first year of price cap regulation, far exceeded the Commission-prescribed rate of return for LEC interstate access services.

aware of the implications of its decision to operate under price caps.⁸

Citizens cannot now plead ignorance of the submissions in the ongoing LEC price cap proceeding (which proposed significant X-Factor increases), of the likelihood of a Commission decision therein within the coming year, and of the past Commission price cap decisions (which required uniform X-Factor treatment for all participating price cap LECs) as an excuse for its price cap election in mid-1996. Citizens has provided no

⁸ When Citizens made its price cap election, it also should have known that the Commission's Rules precluded LECs, which had elected to be subject to price cap regulation, from withdrawing from such regulation. See 47 C.F.R. § 61.41(d).

Although Citizens benefited greatly in its first year of price cap participation, it now complains vehemently that application of the 6.5 percent X-Factor to it would cause its earnings to decline and possibly impair its ability to attract capital. See Citizens Pet. at 11-15. There are several flaws in Citizens' claims in this regard: (1) the magnitude of its projected earnings decline is pure conjecture, and even Citizens admits that it has been "incorrect" in predicting lower earnings in the past (Pet. Att. 2 at 7-8); (2) it does not ascribe its earnings downturn entirely to the new X-Factor, but also attributes it to "other FCC actions" such as newly adopted universal service and access reform requirements (*id.* at 16; Citizens Pet. at 11); (3) it is unclear whether some of its projected earnings decline may be due to Citizens' sharing refunds for excessive earnings in the 1996-97 tariff year; and (4) despite its complaints about the low-end adjustment (Pet. at 9-10), Citizens' own figures (which may be unduly pessimistic) do not show that its return level will fall below 10.25 percent for the full tariff year 1997-98 (see Att. 2 at 7-8), which is the threshold required for a low-end adjustment.

reason to give it special treatment and exempt it from application of the Commission's newly determined X-Factor.

CONCLUSION

For the reasons stated above, the petitions for reconsideration filed by Cincinnati Bell Telephone Company and Citizens Utilities Company should be denied.

Respectfully submitted,

AT&T CORP.

By /s/ Peter H. Jacoby
Mark C. Rosenblum
Peter H. Jacoby

295 North Maple Avenue
Room 3250J1
Basking Ridge, NJ 07920
(908) 221-4243

Jules M. Perlberg

One First National Plaza
Chicago, IL 60603
(312) 853-7439

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CERTIFICATE OF SERVICE

I, Ann Marie Abrahamson, do hereby certify that on this 18th day of August, 1997, a copy of the foregoing "AT&T Opposition to Petitions for Reconsideration" was mailed by U.S. first class mail, postage prepaid, to the parties listed below.

Christopher J. Wilson
Frost & Jacobs LLP
2500 PNC Center
201 East Fifth Street
Cincinnati, OH 45202
Attorneys for Cincinnati Bell
Telephone Company

Thomas E. Taylor
Sr. Vice President-General Counsel
Cincinnati Bell Telephone Company
201 East Fourth St., 6th Floor
Cincinnati, OH 45202

Richard M. Tettelbaum
Associate General Counsel
Citizens Utilities Company
1400 16th St., NW, Suite 500
Washington, D.C. 20036

/s/ Ann Marie Abrahamson
Ann Marie Abrahamson